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Date:

November 05, 2012

TY:

Legend

Distributing =

Controlled =

A

1 =

Shareholder 1 =

Shareholder 2 =

Shareholder 3 =

Shareholder 4 =

a =

b =

c =

d =

e =

f =

Dear :

This letter responds to your June 13, 2012 request for rulings on certain federal income tax consequences of a series of proposed transactions. The information submitted in that letter and in subsequent correspondence is summarized below.

The rulings contained in this ruling letter are based on facts and representations submitted by the taxpayer and accompanied by a penalties of perjury statement executed by the appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process.

In particular, this office has not reviewed any information pertaining to and has made no determination regarding whether the distribution described below: (i) satisfies the business purpose requirement of section 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation (see section 355(a)(1)(B) of the Internal Revenue Code and Treas. Reg. § 1.355-2(d)); or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will directly or indirectly acquire stock representing a 50% or greater interest in the distributing corporation or a controlled corporation (see § 355(e)(2)(A)(ii) and Treas. Reg. § 1.355-7).

FACTS

Distributing is an S corporation incorporated in Year 1 that has one class of common stock outstanding. Distributing is owned by Shareholders 1 through 4 (the "Shareholders"), who own a, b, c, and d shares of common stock Distributing, respectively. The Shareholders are all U.S. residents for federal income tax purposes.

Distributing will form a wholly-owned subsidiary, Controlled, in anticipation of the Distribution, defined below. Controlled will have a single class of common stock outstanding, which will initially be held by Distributing. Distributing and Controlled will both use the same method of accounting and the same taxable year.

Distributing has submitted financial and employment information indicating that it is actively engaged in the A business and had gross receipts and operating expenses representing the active conduct of a trade or business for each of the past five years.

To facilitate one or more of the following corporate business purposes, Shareholders 1 and 2 ("Group 1") and Shareholders 3 and 4 ("Group 2") propose to separate their interests in Distributing through the Proposed Transaction: to enable themselves to independently own and manage separate businesses in accordance with their own goals and priorities, and to restrict each set of shareholders' investment and focus their attention on their own separate business (together, the "Business Purposes").

PROPOSED TRANSACTION

For what have been represented to be valid business purposes, the following series of transactions has been proposed:

- (i) Distributing will form Controlled and transfer to it e% of Distributing's active trade or business assets (the "Contribution"). In exchange, Distributing will receive all of Controlled's outstanding stock.
- (ii) Distributing will distribute to Shareholders 3 and 4 c and d shares of Controlled stock, respectively, in exchange for their respective stock interests in Distributing (the "Distribution").
- (iii) Immediately after the Distribution, Controlled will make an election under section 1362(a) to be treated as an S corporation (within the meaning of section 1361(a)).

After the Distribution, Group 1 will hold all of the outstanding stock of Distributing, which will remain actively engaged in its historic trade or business using the remaining f% of the historic business assets. Group 2 will hold all of the outstanding stock of Controlled, which will be actively engaged in the same trade or business using the e% of the historic Distributing business assets received in the Contribution.

REPRESENTATIONS

- (a) Any indebtedness owed by Controlled to Distributing after the Distributions will not constitute stock or securities.
- (b) Controlled will not transfer any property or assets to Distributing in the Proposed Transaction except for its own stock.

- (c) The fair market value of the Controlled stock to be received by Shareholders 3 and 4 will be approximately equal to the fair market value of the Distributing stock surrendered by each such shareholder in the Distribution.
- (d) No part of the consideration to be distributed by Distributing will be received by a shareholder as a creditor, employee, or in any capacity other than that of a shareholder of Distributing.
- (e) Distributing and Controlled will, both before and after the Distribution, each have only one class of common stock and will have no security holders.
- (f) The five years of financial information submitted on behalf of Distributing is representative of the corporation's present operations and with regard to such corporation there have been no substantial operational changes since the date of the last financial statements submitted.
- (g) Following the Distributions, Distributing and Controlled will each continue the active conduct of their respective businesses, independently and with their separate employees and separate post-Distribution assets.
- (h) The Distribution is carried out for the Business Purposes. The Distribution is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (i) The Distribution is not being used principally as a device for the distribution of the earnings and profits of Distributing, Controlled, or both.
- (j) The total adjusted basis, and the total fair market value, of the assets transferred to Controlled will each equal or exceed the total liabilities assumed (as determined under section 357(d)) by Controlled.
- (k) The liabilities assumed (as determined under section 357(d)) in the transaction and the liabilities to which the transferred assets are subject, if any, were incurred in the ordinary course of business and are associated with the assets being transferred.
- (l) Immediately after the Distribution, the aggregate fair market value of the assets of Controlled will exceed Controlled's aggregate adjusted basis in these assets and will also exceed the amount of liabilities assumed by Controlled (as determined under section 357(d)).
- (m) The income tax liability for the taxable year in which investment credit property (including any building to which section 47(d) applies) is transferred will be adjusted pursuant to section 50(a)(1) or (a)(2) (or section 47, as in

effect before the amendment by Public Law 101-508, Title 11, 104 Stat. 1388, 536 (1990), if applicable) to reflect an early disposition of the property.

- (n) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the Proposed Transaction.
- (o) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution.
- (p) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled will be for fair market value based on terms and conditions arrived at by the parties bargaining at arm's length.
- (q) No two parties to the transaction are investment companies as defined in section 368(a)(2)(F)(iii) and (iv).
- (r) The Distribution is not part of a plan or series of transactions (within the meaning of Treas. Reg. § 1.355-7) pursuant to which one or more persons will acquire, directly or indirectly, stock representing a 50% or greater interest (within the meaning of section 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).
- (s) Neither Distributing nor Controlled will be a disqualified investment corporation (within the meaning of section 355(g)(2)).
- (t) For purposes of section 355(d), immediately after the Proposed Transaction, no person (determined after applying section 355(d)(7)) will hold stock possessing 50% or more of the total combined voting power of all classes of Distributing stock entitled to vote, or 50% or more of the total value of shares of all classes of Distributing stock, that was acquired by purchase (as defined in section 355(d)(5) and (8)) during the 5-year period (determined after applying section 355(d)(6)) ending on the date of the Distributions.
- (u) For purposes of section 355(d), immediately after the Proposed Transaction, no person (determined after applying section 355(d)(7)) will hold stock possessing 50% or more of the total combined voting power of all classes of Controlled stock entitled to vote, or 50% or more of the total value of shares of all classes of Controlled stock, that was either: (i) acquired by purchase (as defined in section 355(d)(5) and (8)) during the 5-year period (determined after applying section 355(d)(6)) ending on the date of the Distribution, or (ii) attributable to distributions on Distributing's stock or securities that were acquired by purchase (as defined in section 355(d)(5) and (8)) during the five-year period (determined after applying § 355(d)(6)) ending on the date of the Distribution.

- (v) Distributing, Controlled, and their respective shareholders will each pay their respective expenses, if any, incurred in connection with the Proposed Transaction, except that Distributing will pay all expenses relating to: (i) the incorporation of Controlled, (ii) the Contribution, (iii) planning and documenting the Proposed Transaction, and (iv) this private letter ruling request.
- (w) Distributing is an S corporation (within the meaning of section 1361(a)). Controlled will elect to be an S corporation pursuant to section 1362(a) on the first available date after its formation, and there is no plan or intent to revoke or otherwise terminate the S corporation status of either Distributing or Controlled.

RULINGS

Based solely on the information submitted and representations set forth above, we rule as follows:

- (1) The Contribution by Distributing to Controlled in exchange for all of the Controlled stock followed by the Distribution will constitute a reorganization within the meaning of section 368(a)(1)(D). Distributing and Controlled each will be a party to a reorganization within the meaning of section 368(b).
- (2) No gain or loss will be recognized by Distributing on its receipt of Controlled stock (sections 361(a) and 357(a)).
- (3) No gain or loss will be recognized by Controlled on the Contribution (section 1032(a)).
- (4) Controlled's basis in each asset received from Distributing in the Contribution will equal the basis of such asset in the hands of Distributing immediately before the Proposed Transaction (section 362(b)).
- (5) Controlled's holding period in each asset received from Distributing in the Contribution will include the holding period during which Distributing held such asset (section 1223(2)).
- (6) No gain or loss will be recognized by Distributing on the Distribution (section 361(c)).
- (7) Shareholders 3 and 4 will not recognize gain or loss (and will include no amount in income) upon their receipt of Controlled stock from Distributing (section 355(a)(1)).

- (8) The adjusted bases of the Controlled stock in the hands of Shareholders 3 and 4 will respectively equal their adjusted bases in the Distributing stock surrendered in exchange thereof, as adjusted under Treas. Reg. § 1.358-1 (section 358(a)(1)).
- (9) The respective holding periods of the Controlled stock to be received by Shareholders 3 and 4 will include the holding periods during which Shareholders 3 and 4, respectively, held the Distributing stock exchanged therefor, provided that the Distributing stock is held as a capital asset on the date of the Distribution (section 1223(1)).
- (10) Distributing's earnings and profits, if any, will be allocated between Distributing and Controlled in accordance with section 312(h) and Treas. Reg. § 1.312-10(a).
- (11) If applicable, the accumulated adjustments account of Distributing will be allocated between Distributing and Controlled in a manner similar to the manner in which the earnings and profits of Distributing will be allocated under section 312(h) (see Treas. Reg. § 1.312-10(a) and Treas. Reg. § 1.1368-2(d)(3)).
- (12) Provided that the Distribution is undertaken immediately after the Contribution and issuance of Controlled stock, Distributing's momentary ownership of the stock in Controlled, as part of the reorganization under section 368(a)(1)(D), will not cause Controlled to have an ineligible shareholder for any portion of its first taxable year under section 1361(b)(1)(B) and will not, in itself, render Controlled ineligible to elect to be an S corporation for its first taxable year.

CAVEATS

Except as expressly provided herein, no opinion is expressed about the tax treatment of the Proposed Transaction or any other transaction or item mentioned in this letter under other provisions of the code or regulations, or about the tax treatment of any conditions existing at the time of, or effects resulting from, the foregoing that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding: (i) whether the Distribution satisfies the business purpose requirement of Treas. Reg. § 1.355-2(b); (ii) whether the Distribution is used principally as a device for the distribution of the earnings and profits of Distributing, Controlled, or both; or (iii) whether the Distribution is part of a plan (or a series of related transactions) under section 355(e)(2)(A)(ii).

In addition, no opinion is expressed about the validity of any S corporation election or the continuing eligibility for S corporation status of either Distributing or Controlled, except as provided herein. No opinion is expressed about whether the stock

of Distributing and Controlled constitute capital assets in the hands of their holders. Furthermore, no opinion is expressed for Federal employment tax purposes regarding the employment status or reasonable compensation of individuals represented by Taxpayer to perform managerial and/or operational services as employees or as independent contractors of Distributing or Controlled either prior to, or subsequent to the Proposed Transaction which is the subject of this letter ruling request.

PROCEDURAL STATEMENTS

This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Isaac W. Zimbalist

Isaac W. Zimbalist
Senior Technician Reviewer, Branch 5
Office of Associate Chief Counsel
(Corporate)

cc: